SYARIKAT IBRACO-PEREMBA SDN BHD v. KETUA PENGARAH HASIL DALAM NEGERI

COURT OF APPEAL, PUTRAJAYA
ABDUL WAHAB PATAIL JCA
LINTON ALBERT JCA
UMI KALTHUM ABDUL MAJID JCA
[CIVIL APPEAL NO: W-01-177-04-2013]
29 MAY 2014

REVENUE LAW: *Income tax – Tax avoidance – Property development company – Sale of property to subsidiary company – Profit derived from sale – Whether subject to tax – Method of calculation – Whether appellant sold shares held in subsidiary company – Whether properties sold to third party before subsidiary wound up – Whether respondent invoked s. 140 Income Tax Act 1967 to impose tax on appellant's transactions for sale of property and shares – Whether transactions preordained – Whether Special Commissioner of Income Tax considered appellant's transaction where income was produced – Whether transactions viewed as a whole – Whether incidence of tax altered – Whether respondent has discretion to impose penalty under s. 113(2)*

REVENUE LAW: *Income tax – Special Commissioners – Findings of – Appeal against decision – Role of appellate court – Whether findings of primary facts by Special Commissioner unassailable – Whether decision of Special Commissioner upheld – Chu Lip Kong v. Director-General of Inland Revenue*

The appellant was a property development company which purchased, developed and sold lands. The profits derived were regarded as business income and were subjected to income tax under the Income Tax Act 1967 ('the Act'). In 1992, the appellant intended to build shop houses and complex on the lands for long term investment purposes. The appellant sought the advice from Arthur Andersen HRM (Tax Services) ('Arthur Andersen') and the former was advised to set up a subsidiary and thereafter sell the lands to the said subsidiary. Based on the advice, the appellant formed a realty company known as Ibraco-Peremba Holdings Sdn Bhd ('IPH') as a wholly owned subsidiary of the appellant and sold its lands to IPH ('first transaction'). Ibraco Bhd ('Ibraco'), a related company of the appellant, held 60.5% shares in Vendu Sdn Bhd ('Vendu') while another 39.5% was held by Peremba Holdings Sdn Bhd ('Peremba'). IPH then entered into a Turnkey Construction Contract with the appellant to develop the lands. The project was completed in 1996 which comprised of 23 shop houses, one shopping complex and one office building. The properties were then rented out and the income derived from it was declared as the business income of IPH. Pursuant to a corporate restructuring exercise, the appellant sold the shares in IPH to Vendu ('second transaction'). On 11 June 2003,

the appellant disposed its shares in IPH to Vendu for a consideration of RM22.5 million. Thereafter, IPH and Vendu were voluntarily wound up after completion of the sale of the properties to third parties ('third transaction'). The facts revealed that the profit from the said disposal was determined based on the value of the transfer of the appellant's shares in IPH to Vendu, *ie*, RM22.5 million by deducting the investment cost incurred by the appellant in IPH. The respondent reviewed the method of determining the profit which was based on the total value of the disposal of the properties, *ie*, RM29,140 by deducting the development cost incurred for the project. By applying the new method, the net profit of the appellant from the said proposal was RM13,518,620. In conjunction with that, the respondent later issued a reduced assessment against the appellant which stated that the amount of RM1,893,572.80 had been discharged. On 30 November 2006, the respondent raised the additional assessment on the profit or surplus of RM16,900,000. Dissatisfied, the appellant appealed to the Special Commissioner of Income Tax ('SCIT') and it was decided, *inter alia*, that (i) the respondent was right to invoke s. 140 of the Act to impose the tax on such transaction; and (ii) the imposition of the penalty against the appellant under s. 113(2) of the Act was correct in law. The appellant's appeal ('the deciding order') was therefore dismissed. Similarly, the appellant's appeal to the High Court was dismissed. It was decided that the facts found by the SCIT were unassailable on appeal and could not be overruled or supplemented except in certain circumstances. Hence, this appeal. The appellant argued that s. 140 of the Act was not applicable and it was not liable to pay the tax of its former subsidiary. Further, it was contended that for s. 140 to be applicable, there had to be a transaction which consisted of several legal documents and sub-transactions which must have been a preordained series of transactions. In this context, the appellant submitted that the word "preordained" implied that the second and third transactions must have been in the mind of the appellant at the time of the first transaction. Those transactions, as alleged, could not be said to be preordained when the transactions were separated in time by nine years. The issues that arose for consideration were (a) whether s. 140(1)(a) of the Act applied to the appellant; and (b) whether the penalty under s. 113(2) of the Act was automatically imposed by the respondent against the appellant.

Held (dismissing appeal with costs)

Per Umi Kalthum Abdul Majid JCA delivering the judgment of the court:

(1) In every case stated for the opinion of the High Court, the Special Commissioners should state clearly and explicitly what are the findings of fact upon which their decision is based and not the evidence upon which those findings, so far as they consist of primary facts, are founded. Findings of primary facts by the Special Commissioners are unassailable. They can neither be overruled nor supplemented by the

High Court itself. Occasionally, they may be insufficient to enable the High Court to decide the question of law sought to be raised by the case stated but in that event, it will be necessary for the case to be remitted to the Commissioners themselves for further findings. It is the primary facts so found by the Commissioners that they should set out in the case stated as having been admitted and/or proved (*Chu Lip Kong v. Director-General of Inland Revenue*; refd). (para 10)

(2) It is for the taxpayer to demonstrate that the transaction or the arrangement by which the income was produced was so preordained by compliance with the requirements of law or accepted business practices to limit risk exposure and that the tax saving were purely incidental. The taxpayer's tax advantage is not derived from an arrangement but from the reduction of income which he accepts by reducing his income or the higher expenditure which he incurs or by incurring expenditure in circumstances in which the taxing statute affords a reduction in tax liability (*Commissioner of Inland Revenue v. Challenge Corporation Ltd*; refd). (paras 28 & 29)

(3) There was no error of law committed by the learned judge when she dismissed the appellant's appeal and affirmed the SCIT's deciding order. The advice of Arthur Andersen was obtained for the primary purpose of ordering the transactions in a manner to minimise tax. The facts found by the SCIT showed that there was tax avoidance when the transactions entered into by the appellant through shell companies revealed the factual situation that the tax position was, *inter alia*, altered. (paras 30 & 31)

(4) The learned judge found that the SCIT committed no error to warrant intervention as there were evidence and facts to support the findings of the SCIT in arriving at the decision they did and hence, justified a case under s. 140 of the Act. The second and third transactions were in discharge of the scheme advanced by Arthur Andersen as a way of avoiding tax by the appellant, notwithstanding the long passage of time. There was a comparatively long period of time of about five years in its proposal before the properties could be disposed off. The fact that the respondent only discovered in 2005 about the tax advice given by Arthur Andersen became significant. (paras 32 & 33)

(5) Section 113(2) of the Act gives a discretion to the respondent to impose a penalty on a person who has failed to observe the requirements of the law as provided in para. 2(a) or (b) of s. 113. There is a distinction between s. 113(1) and 113(2) of the Act. The defence of good faith as found in s. 113(1) and not found in s. 113(2) does not apply to the Director General's discretion under s. 113(2). Section 140 does not expressly or impliedly exclude the operation of s. 113. Section 140 gives the discretion to the respondent in certain circumstances and did

not relate to a question of breach by the appellant. Neither does the provisions of s. 113 excludes its application in the circumstances provided for under s. 140. On the facts, if not for the fact that an investigation had been carried out on the appellant and it had stumbled upon the Arthur Andersen's tax advice in 2005, the scheme would never had seen the light of day. As such, the respondent did not err for invoking s. 113(2) against the appellant. (paras 40 & 41)

Case(s) referred to:

Chu Lip Kong v. Director-General of Inland Revenue [1982] CLJ 398; [1982] CLJ (Rep) 1 PC ***(refd)***

Commissioner of Inland Revenue v. Challenge Corporation Ltd [1986] STC 548 ***(refd)***

Director-General of Inland Revenue v. Rakyat Berjaya Sdn Bhd [1984] 1 CLJ 219; [1984] 1 CLJ (Rep) 108 FC ***(refd)***

Edwards v. Bairstow & Harrison 36 TC 207; [1956] AC 14 ***(refd)***

Ensign Tankers (Leasing) Ltd v. Stokes (Inspector of Taxes) [1992] 1 AC 655 HL ***(refd)***

Furniss (Inspector of Taxes) v. Dawson and Related Appeals [1984] STC 153 HL ***(refd)***

IRC v. Duke of Westminster [1936] AC 1 ***(refd)***

Ketua Pengarah Hasil Dalam Negeri v. Kim Thye & Co [1992] 4 CLJ 2079; [1992] 1 CLJ (Rep) 135 SC ***(refd)***

Lauri Joseph Newton and Ors v. Commissioner of Taxation of the Commonwealth of Australia [1958] AC 450 PC ***(refd)***

Lower Perak Co-Operative Housing Society Bhd v. Ketua Pengarah Hasil Dalam Negeri [1994] 3 CLJ 541 SC ***(refd)***

Sabah Berjaya Sdn Bhd v. Ketua Pengarah Jabatan Hasil Dalam Negeri [1999] 3 CLJ 587 CA ***(refd)***

Simmons (as liquidator of Lionel Simmons Properties Ltd) v. Inland Revenue Commissioners [1980] STC 350 ***(refd)***

WT Ramsay Ltd v. Inland Revenue Commissioners [1981] 1 All ER 865; [1982] AC 300 HL ***(refd)***

Legislation referred to:

Income Tax Act 1967, ss. 113(1)(a), (b), (2)(a), (b), 140(1)(a), (c)
Interpretation Acts 1948 and 1967, s. 17A
Real Property Gains Tax Act 1976, s. 7

Income Tax Act 1976 [NZ], s. 99

For the appellant - WSW Davidson (Francis Tan & Cheah Keng Soon with him); Azman Davidson & Co

For the respondent - Abu Tariq Jamaluddin (Ashrina Ramzan Ali & Hasniza Alias with him); LHDN

[Appeal from High Court, Kuala Lumpur; Appellate and Special Powers Division No: R2-14-17-2011].

Reported by Kumitha Abd Majid

JUDGMENT

Umi Kalthum Abdul Majid JCA:

[1] This is an appeal to this court by the appellant against the decision of the High Court dated 5 April 2013 in respect of the appellant's requisition against the deciding order by the Special Commissioners of Income Tax ("SCIT").

Facts

[2] The brief facts of the case as found by the SCIT (para. 6(a)-(r), case stated, pp. 32-35, RR Bahagian A&B) are as follows:

(a) the appellant is a property development company. The appellant buys land, develops the land and sells them. Any profits arising therefrom are regarded as business income and are subjected to income tax under the Income Tax Act 1967 ("the Act");

(b) sometime in 1992, the appellant identified the properties held under Lots 8874 to 8918, Muara Tebas Land District, Bandar Kuching (hereinafter referred to as "the lands") as being suitable for long term investment. It intended to build shophouses and complex on the lands in its entirety or in units. The appellant also planned to build shophouses on another lot of land with the objective of leasing out the shophouses for a period of time prior to sale (the lands together with the completed commercial buildings hereinafter referred to as "the properties");

(c) the appellant sought the advice from Arthur Andersen HRM (Tax Services) Sdn Bhd ("Arthur Andersen"). The advice received was to the effect that the appellant should set up a subsidiary and thereafter sell the lands to the subsidiary;

(d) based on the advice, the appellant formed a realty company Ibraco-Peremba Holdings Sdn Bhd ("IPH"). IPH was a wholly owned subsidiary of the appellant and it was incorporated on 5 January 1994. The principal activity of IPH was investment holding and property developer;

(e) Ibraco Bhd ("Ibraco") held 60.5% shares in Vendu Sdn Bhd ("Vendu") while another 39.5% was held by Peremba Holdings Sdn Bhd ("Peremba");

(f) after the sale of the lands by the appellant to IPH, IPH entered into the turnkey construction contract on 27 August 1994 with the appellant to develop the lands;

(g) the project was completed around the year 1996. It comprised of 23 shophouses, one shopping complex known as Wisma Wan and one office building known as Ibraco House. Apart from that, based on IPH audited account for year ending 31 January 1997, IPH fixed asset was valued at RM13,422,700;

(h) after the completion of the said project, it was rented out and rental income was declared as IPH business income;

(i) pursuant to a corporate restructuring exercise, the appellant sold the shares in IPH to Vendu on 11 June 2003. The shareholders of Vendu were Ibraco, a related company of the appellant, and Peremba. The ratio of shareholding was 60.5% and 39.5% respectively;

(j) from the respondent's data base system, the directors of Vendu were:

(i) Ravindranatham a/l KP Kasavapillai (employee of Peremba Development Sdn Bhd) and holds 39.5% of share holding;

(ii) Vijayalingam a/l Vythilingam; and

(iii) Angela Liew Siaw Fan (employee of Ibraco) and holds 60.5% of share holding;

(k) on 11 June 2003, the appellant disposed its shares in IPH to Vendu for the consideration of RM22.5 million;

(l) after the change in shareholdings in IPH, IPH sold "the properties" in 2003 and 2004 realising a gain of RM16,900,000;

(m) initially, the profit from the said disposal was determined based on the value of the transfer of the appellant's share in IPH to Vendu, that is, RM22.5 million by deducting the investment cost incurred by the appellant in IPH, that is, RM5.6 million. Hence, the net income was RM16.9 million;

(n) after reviewing the abovesaid basis, the respondent reviewed the method in determining the profit, which was based on the total value of the said disposal, that is, RM29,140,000 by deducting the development cost incurred on the project, that is, RM15,621,380. By applying the new method, the net profit of the appellant from the said proposal was RM13,518,620;

(o) in conjunction with that, the respondent had later issued a reduced assessment dated 16 January 2008 against the appellant which stated that the amount of RM1,893,572.80 had been discharged;

(p) on 30 November 2006 the respondent raised the additional assessment on the profit or surplus of RM16,900,000. The appellant appealed to the SCIT for determination;

(q) through its resolution, IPH was voluntarily wound up; and

(r) Vendu too was voluntarily wound up and upon liquidation, all of Vendu's assets were passed to its shareholders who were nominees of Ibraco and Peremba.

Contentions Before SCIT

[3] Before the SCIT, the appellant contended that it had disposed of only the lands upon which was constructed 23 shop lots, Wisma Wan and Ibraco House and that it had only sold 5,600,000 shares in IPH. The disposal of shares in IPH was a realisation of investment and not an adventure in the nature of trade or trading. If there is a liability to tax it should be on the gain arising from the disposal of shares in a real property company, pursuant to Sch. 2, s. 7, para. 34A of the Real Property Gains Tax Act 1976 ("RPGT Act"). Further, the sale was at market value.

[4] The appellant further contended that it should not be held liable to pay tax on the profit made by its subsidiary, otherwise the appellant would then be liable to pay tax twice - once when it sold the lands to IPH in 1994 and then again be responsible for tax of IPH. The appellant contended that the respondent was not justified n invoking s. 140 of the Act.

[5] The respondent contended that the appellant should be taxed under the Act in respect of the proceeds from the disposal of the commercial buildings which contained 23 shop lots, Wisma Wan and Ibraco House which had been developed by the appellant. The assessment was not raised on the disposal of shares in IPH. It was submitted that based on the facts and the law, the respondent had correctly exercised his discretion to invoke s. 140 of the Act, where disposal of the lands to IPH had been disregarded under that section and adjustment was made to bring to tax all proceeds from the disposal of the properties as income of the appellant. The respondent had also correctly exercised his discretion to impose penalty under s. 113(2) of the Act.

[6] After a full hearing, the SCIT decided that the respondent was right to invoke s. 140 of the Act and to impose the tax on such transaction. The SCIT also decided that the imposition of the penalty by the respondent under s. 113(2) of the Act was correct in law and had unanimously dismissed the appellant's appeal ("the deciding order"). The appellant then appealed to the High Court against the deciding order.

Appeal At The High Court

[7] On appeal to the High Court, the deciding order of the SCIT was upheld and the appeal of the appellant was dismissed. The learned High Court Judge ruled that the facts found by the SCIT were unassailable on appeal and it could not be overruled or supplemented except in certain circumstances. The learned judge held that there was no error committed

by the SCIT to warrant interference of the High Court as there were evidence and facts to support the findings of the SCIT in arriving at their decision.

[8] The appellant now appeals to this court.

The Appeal

Role Of An Appellate Court In A Tax Appeal

[9] Before addressing the appeal at hand, we remind ourselves on the position of law on the role of an appellate court in a tax appeal based on decided cases. Counsel for the respondent had cited *Chu Lip Kong v. Director-General of Inland Revenue* [1982] CLJ 398; [1982] CLJ (Rep) 1; [1982] 1 MLJ 235; *Edwards v. Bairstow and Harrison* 36 TC 207 T; [1956] AC 14, and *Lower Perak Co-Operative Housing Society Bhd v. Ketua Pengarah Hasil Dalam Negeri* [1994] 3 CLJ 541; [1994] 3 BLJ 265 to this end. The Supreme Court in *Lower Perak Co-operative Housing Society Bhd* had adopted the principles enunciated by Lord Radcliffe in *Edwards v. Bairstow and Harrison* regarding the duty of the court when hearing appeals from commissioners in tax cases, at p. 35, as follows:

> ... When the case comes before the Court it is its duty to examine the determination having regard to its knowledge of the relevant law. If the case contains anything *ex facie* which is bad law and which bears upon the determination, it is, obviously, erroneous in point of law. But, without any such misconception appearing *ex facie* it may be that the facts found are such that no person acting judicially and properly instructed as to the relevant law could have come to the determination under appeal. In those circumstances, too, the Court must intervene. It has no option but to assume that there has been some misconception of the law and that this has been responsible for the determination. So there, too, there has been error in point of law. I do not think that it much matters whether this state of affairs is described as one in which there is no evidence to support the determination or as one in which the evidence is inconsistent with and contradictory of the determination, or as one in which the true and only reasonable conclusion contradicts the determination. Rightly understood, each phrase propounds the same test. For my part, I prefer the last of the three, since I think that it is rather misleading to speak of there being no evidence to support a conclusion when in cases such as these many of the facts are likely to be neutral in themselves, and only to take their colour from the combination of circumstances in which they are found to occur.

[10] We do not wish to add further to that enunciation on the principles of law on the subject. We, however, would like to note the principles as enunciated by the Privy Council in *Chua Lip Kong*'s case (*supra*) at p. 236 para. B, left, with regard to the findings of facts by the SCIT as follows:

> Their Lordships cannot stress too strongly how important it is that, in every Case Stated for the opinion for the opinion of the High Court, the Special Commissioners should state clearly and explicitly what are the findings of fact upon which their decision is based and not the evidence upon which those findings, so far as they consist of primary facts, are founded. Findings of primary facts by the Special Commissioners are unassailable. They can be neither overruled nor supplemented by the High Court itself; occasionally they may be insufficient to enable the High Court to decide the question of law sought to be raised by the Case Stated, but in that event it will be necessary for the Case to be remitted to the Commissioners themselves for further findings. It is the primary facts so found by the Commissioners that they should set out in the Case Stated as having been "admitted and or proved".

[11] Bearing in mind these principles, we now come to our decision on the appeal.

Issues

[12] Before us, the appellant had raised two issues, namely:

(a) whether s. 140(1)(a) of the Act applied to the appellant; and

(b) whether the penalty under s. 113(2) of the Act was automatically imposed on the appellant by the respondent.

Section 140(1)(a)

Appellant's Case

[13] The appellant raised the arguments that s. 140 of the Act was not applicable to the appellant and the appellant was not liable to pay the tax of its former subsidiary and that it had not undertaken tax avoidance exercise thereby enabling the respondent to invoke this section.

[14] To illustrate its arguments the appellant in its written submission drew up a diagram in Appendix A showing there were three transactions involving the properties. The first transaction was for the sale of the lands from the appellant to its own subsidiary IPH, pursuant to scenario B of Arthur Andersen's advice. This transaction took place in 1994. In the same year, IPH entered into a turnkey construction contract with the appellant to develop the lands ("the project"). The costs were based on actual costs of development and construction up to completion together with a 6.5% management fee. The project was completed in 1996. Upon the completion of the project the buildings were rented and rental income was declared as business income of IPH. When the lands were sold to IPH in 1994, the appellant ceased to be owners of the lands. Therefore the later transactions, that is, the second and third transactions were not at all within the contemplation at that time. The second and third transactions were separated in time from the first transaction by about nine years.

[15] The second transaction was when the appellant sold its shares in IPH to Vendu on 11 June 2003 for the sum of RM22,500,000. The appellant's explanation for this course of action was that it had sought to have its shares listed in the Kuala Lumpur Stock Exchange through a newly set up holding company Ibraco Berhad. Upon advice from its financial advisers, that IPH should be excluded from the listing scheme to avoid adverse effect on the price of the listed shares, it was decided that IPH needed to cease to be a wholly owned subsidiary of the appellant. However, payment for the shares was deferred and evidenced by promissory notes. It was not disputed that the beneficial owner of Vendu were the same persons as were the owners of the appellant's shares prior to the listing.

[16] Further, for the purpose of tax, the sale of the IPH shares would be classified as a sale of a chargeable asset pursuant to para. 34A of the Second Schedule to the RPGT Act. However, the RPGT Act was suspended from its application from 1 June 2003 till 31 May 2004 *vide* Real Property Gains Tax (Exemption) (No. 2) Order 2003. This meant that vendors of chargeable assets (namely the appellant) within the meaning if the RPGT Act were entirely fee to dispose of their assets without the gain being subjected to tax. If a person took advantage of this suspension (as did the appellant it was argued) to dispose of chargeable assets and avoid paying tax, this is a clear example of permissible tax mitigation and the respondent had no right to seek to recover the revenue thereby lost by invoking s. 140 of the Act.

[17] The third transaction was the sale of the properties by IPH to third parties unrelated to the appellant in August 2003 to July 2004. IPH and Vendu were then voluntarily wound up after the sale of the properties had been completed. It was the appellant's contention that the voluntary winding up of IPH and Vendu were natural processes whereby when IPH (now a subsidiary of Vendu) had sold all its properties, it was wound up. The assets of IPH consisting of the proceeds from the sale then passed to Vendu which in turn used the money to pay the appellant for the IPH shares sold by the appellant to Vendu but which Vendu had not paid for the shares yet.

[18] It was further submitted that the appellant was entitled to minimise the tax to be paid to the respondent if the appellant was able to manage to organise it business to that effect. The appellant referred to the New Zealand case of *Commissioner of Inland Revenue v. Challenge Corporation Ltd* [1986] STC 548 at p. 554 (which involved the interpretation of s. 99 of the New Zealand Income Tax Act 1976 which is in *pari materia* with section 140 of the Act), per Lord Templeman:

> The material distinction in the present case is between tax mitigation and tax avoidance. A taxpayer has always been free to mitigate his liability to tax. In the oft quoted words of Lord Tomlin in *IRC v. Duke of Westminster* [1936] AC 1 at 19, 19 TC490 at 520.

> Every man is entitled if he can to order his affairs so as that the tax attaching under the appropriate Act is less than it otherwise would be'. In that case however the distinction between tax mitigation and tax avoidance was neither considered nor implied.
>
> Income tax is mitigated by a taxpayer who reduces his income or incurs expenditure in circumstances which reduce his assessable income or entitle him to reduction in his tax liability. Section 99 does not apply to tax mitigation because the taxpayer's tax advantage is not derived from an 'arrangement' but from the reduction of income which he accepts or the expenditure which he incurs.
>
> [At p. 555] Section 99 does not apply to tax mitigation where the taxpayer obtains a tax advantage by reducing his income or by incurring expenditure in circumstances in which the taxing statute affords a reduction in tax liability.

[19] Further references were made to *Director-General of Inland Revenue v. Rakyat Berjaya Sdn Bhd* [1984] 1 CLJ 219; [1984] 1 CLJ (Rep) 108; [1984] 1 MLJ 248 FC; *Sabah Berjaya Sdn Bhd v. Ketua Pengarah Jabatan Hasil Dalam Negeri* [1999] 3 CLJ 587; [1999] 3 MLJ 145 CA; *Lauri Joseph Newton and Ors v. Commissioner of Taxation of the Commonwealth of Australia* [1958] AC 450 PC; *Furniss (Inspector of Taxes) v. Dawson and Related Appeals* [1984] STC 153 HL; *Ensign Tankers (Leasing) Ltd v. Stokes (Inspector of Taxes)* [1992] 1 AC 655, HL; *Simmons (as liquidator of Lionel Simmons Properties Ltd) v. Inland Revenue Commissioners* [1980] STC 350; *Lower Perak Co-Operative Housing Society Bhd v. Ketua Pengarah Hasil Dalam Negeri (supra).* These cases were cited by the appellant to support its contention that for s. 140 to have any application there has to be "a transaction", which may consist of several legal documents and "subtransactions" which must have been a "preordained series of transactions". In the context of this case, the word "preordained" implied that the second and the third transactions must have been in the mind of the appellant at the time of the first transaction. These second and third transactions cannot be said to the "preordained" particularly where these transactions were separated in time by nine years.

[20] It was submitted for the appellant that whilst the learned High Court Judge had accepted the *Furniss* test that there must be a preordained series of transactions forming a simple composite transaction, she had erred when she relied on *WT Ramsay Ltd v. Inland Revenue Commissioners* [1981] 1 All ER 865 for the principle that in looking at tax avoidance scheme which comprised a number of specific transactions to avoid tax, the genuineness or otherwise of each individual step or transaction need not be looked at from each individual step or transaction but it is to be looked at as a whole. It was submitted that the learned High Court Judge had erred when she had looked at all the transactions on hindsight and said that there was a scheme. The proper way was for the learned judge to look at the scheme as it was in

1994 and see whether the activities contemplated then conformed with the scheme. Moreover, the learned judge had failed to consider the issue of whether the first, second and third transactions were all preordained and that there was no finding to this effect.

Respondent's Case

[21] It was submitted for the respondent that the appellant is a property development company that buys land, develops the said land and sells them. The profits arising therefrom are business income and as such are subjected to the Act. The appellant had identified the lands as being suitable for long term investments. It had intended to build shophouses and complex on it in its entirety or in units. It had also planned to build shophouses on another lot of land with the objective of leasing out the shophouses for a period of time prior to the sale.

[22] By a letter dated 8 October 1993 from Arthur Andersen, it appeared that the appellant had sought advice to minimise its tax. The salient paragraphs are extracted from the said letter and read as follows:

> Background
>
> We understand that the principal activity of Ibraco-Peremba Sdn. Bhd. (hereinafter "the Company") is developing properties for resale. It intends to build shop-houses and a complex for renting out for a period of time before it sells the shop-houses and complex in its entirety or in units. The company has applied for approval to build the shop-houses and complex.
>
> The Company also plans to build shop-houses on another lot of land with the objective of leasing out the shop-houses for a period of time prior to sale.
>
> Against this background we have been requested to suggest an effective method of developing the properties to minimise the tax impact to the Company.

[23] In the same letter there were two scenarios suggested by Arthur Andersen to minimise tax impact and the appellant had chosen scenario B. The extract of scenario B is reproduced below:

> Under this scenario, we have considered a structure which, if implemented, could result in the sales proceeds being treated as capital gains and hence, be subject to RPGT. That is, the lands will be transferred to a 100% realty company of Ibraco. Real property gains tax is payable on the market surplus of the lands. Stamp duty exemption should be available under Section 15A of the Stamp Act. As the developed properties will be held for rental for a relatively long period, say 5 years, there is a valid argument that the gain (or loss) of the investment properties is on capital account and subject to real property gains tax.

[24] Pursuant to Arthur Andersen's advice, the appellant had incorporated IPH which it owned wholly. The appellant then transferred the lands to IPH. IPH then appointed the appellant by way of power of attorney (p. 231, RR Bahagian C) to deal with the lands. The appellant had also entered into the turnkey construction agreement/contract ("the agreement") with IPH to develop the lands (that is the project) in which the total development costs were to be borne by the appellant (fourth paragraph of the preamble and cl. 4.6 of the agreement, pp. 232, 234, RR Bahagian C). The project was completed in 1996, after which the shophouses, shopping complex and office building were rented out and rental income was declared as IPH business income. The respondent then went on to detail out the various transactions entered into by the appellant and or its associated companies as seen from the facts found by the SCIT which we do not wish to repeat other than the following facts:

(a) when the appellant sold all its shares in IPH to Vendu for the sum of RM22.5 million (pp. 266-279, RR Bahagian C), Vendu had paid the appellant by way of "promissory notes", which meant to say that there was no actual payment of the said sum was made then;

(b) after receiving the "payment" through the "promissory notes", the appellant had declared dividend in kind to its shareholders, namely Ibraco Berhad (RM13,599,754) and Permodalan Peremba Sdn Bhd (RM8,900,246) in its resolution at p. 248, RR Bahagian C;

(c) in the Ibraco Peremba Holdings Sdn Bhd's resolution at p. 249 of the RR Bahagian C, it could be clearly seen that IPH was to be voluntarily wound up;

(d) based on the resolution at p. 253, RR Bahagian C, Vendu too was to be voluntarily wound up.

[25] It was submitted by the respondent that the appellant's intention had remained the same throughout these various transactions, that is, to develop and dispose the properties. The setting up of IPH was merely a vehicle to defray such intention where IPH was fully controlled by the appellant and was without any expertise or funds to develop the properties. There was no commercial nor business reason to set up IPH except for the purpose of the scheme to avoid such disposal from being taxed under income tax. IPH and Vendu were formed for the purpose of disposing the said properties and after they had completed their tasks both had been voluntarily wound up by their shareholders. The effect of the whole scheme was that the profits from the disposal of the said properties went back to the appellant.

[26] The respondent submitted that from the facts, they clearly showed that the scheme adopted by the appellant did not fall within the meaning of organising its affairs so as to minimise tax. The scheme was a tax avoidance scheme and it must fall within the scope of s. 140 of the Act.

The Decision

[27] Section 140 of the Income Tax Act 1967 reads as follows:

> Power to disregard certain transactions
>
> 140. (1) The Director General, where he has reason to believe that any transaction has the direct or indirect effect of:
>
> (a) altering the incidence of tax which is payable or suffered by or which would otherwise have been payable or suffered by any person;
>
> (b) relieving any person from any liability which has arisen or which would otherwise have arisen to pay tax or to make a return;
>
> (c) evading or avoiding any duty or liability which is imposed or would otherwise have been imposed on any person by this Act; or
>
> (d) hindering or preventing the operation of this Act in any respect,
>
> may, without prejudice to such validity as it may have in any other respect or for any other purpose, disregard or vary the transaction and make such adjustments as he thinks fit with a view to counteracting the whole or any part of any such direct or indirect effect of the transaction.

[28] The distinction between what is accepted and what is not in the way of reducing the amount of tax to be paid used to be conveniently described by the terms tax avoidance and tax evasion respectively. Section 140(1)(c) of the Act in particular, has the effect of demolishing that convenient description. The Act now empowers the Director General, without prejudice to such validity as it may have in any other respect or for any other purpose, where he has reason to believe that any transaction has the direct or indirect effect of evading or avoiding any duty or liability which is imposed or would otherwise have been imposed on any person by the Act, to disregard or vary the transaction and make such adjustments as he thinks fit with a view to counteracting the whole or any part of any such direct or indirect effect of the transaction. Thus the oft quoted words of Lord Tomlin in *IRC v. Duke of Westminster* [1936] AC 1 and quoted by Lord Templeman in *Commissioner of Inland Revenue v. Challenge Corporation Ltd (supra)* that every man is entitled if he can to order his affairs so as that the tax attaching under the appropriate Act is less than it otherwise would be is now only partially true, for whether he succeeds or not, according to s. 140(1)(c), depends upon the determination of the Director General. We make the observation that it is for the taxpayer to demonstrate that the

transaction or the arrangement by which the income was produced was so preordained by compliance with the requirements of law or accepted business practices to limit risk exposure, and that the tax savings were purely incidental.

[29] Other than the above all that remains solely at the taxpayer's discretion is "tax mitigation", which as explained by Lord Templeman is not subject to the section because the taxpayer's tax advantage is not derived from an "arrangement" but from the reduction of income which he accepts by reducing his income, or the higher expenditure which he incurs, or by incurring expenditure in circumstances in which the taxing statute affords a reduction in tax liability.

[30] After a careful perusal of the facts as found by the SCIT, and which we agree with the learned High Court Judge's view that those findings of facts should not be disturbed (see *Chu Lip Kong*'s case *supra*), the submissions of the parties as well as the documentary evidence, we are of the view that there is no error of law committed by the learned judge when she dismissed the appellant's appeal and affirmed the SCIT's deciding order.

[31] In this case it is quite clear that the advice of Arthur Andersen was obtained for the primary purpose of ordering the transactions in a manner to minimise tax. We find that based on the factual matrix of this case the learned High Court Judge was not wrong in coming to her conclusion that the facts found by the SCIT showed that there was tax avoidance when the transactions entered into by the appellant through shell companies revealed the factual situation that the tax position was altered; that the SCIT found that the appellant had in fact implemented a scheme following the advice of the tax consultant in perpetuating one original intention of selling of the properties as it intended to do from the start.

[32] The learned High Court Judge had referred to *WT Ramsay Ltd v. Inland Revenue Commissioners* [1981] 1 All ER 865; [1982] AC 300 HL for the principle that in looking at tax avoidance scheme which comprised a number of specific transactions to avoid tax, the genuineness or otherwise of each individual step or transaction need not be looked at from each individual step or transaction but it is to be looked at as a whole. As such the learned judge found there was no error committed by the SCIT to warrant intervention by her as there were evidence and facts to support the findings of the SCIT in arriving at the decision they did and hence justifying a case under s. 140 of the Act. We agree with her reasoning and conclusion.

[33] Contrary to the appellant's submission (that the second and third transactions could not be said to be "preordained" particularly when these transactions were separated in time by nine years, based on the principle enunciated in *Furniss (Inspectors of Taxes) v. Dawson (supra)* and endorsed by *Ensign Tankers (Leasing) Ltd v. Stokes (supra)*, we accept the SCIT's findings

of facts that the so-called second and third transactions were in discharge of the scheme advanced by Arthur Andersen in scenario B as a way of avoiding tax by the appellant, the long passage of time notwithstanding. In any case, scenario B did envisage a comparatively long period of time of about five years in its proposal before the properties could be disposed off. The passage of time is of little consequence in the scheme of things for the appellant when we take into account the findings of facts by the SCIT in para. 2 above and the matters highlighted by the respondent in para. 20 above. To this end, the fact that the tax advice given by Arthur Andersen was only discovered by the respondent in 2005 then becomes significant.

[34] For the reasons stated above, we therefore affirm the High Court Judge's decision affirming the SCIT's decision that s. 140(1)(a) of the Act applied to the appellant.

Penalty Under Section 113(2)

[35] The appellant had also raised the issue of whether or not the respondent was in error in subjecting the appellant to penalties under s. 113(2) of the Act before the High Court, but which was not dealt with explicitly by the learned High Court Judge. They also raised the same issue before us. Section 113 of the Act provides as follows:

> Incorrect returns
>
> 113. (1) Any person who:
>
> (a) makes an incorrect return by omitting or understating any income of which he is required by this Act to make a return on behalf of himself or another person; or
>
> (b) gives any incorrect information in relation to any matter affecting his own chargeability to tax or the chargeability to tax of any other person,
>
> shall, unless he satisfies the court that the incorrect return or incorrect information was made or given in good faith, be guilty of an offence and shall, on conviction, be liable to a fine of not less than one thousand ringgit and not more than ten thousand ringgit and shall pay a special penalty of double the amount of tax which has been undercharged in consequence of the incorrect return or incorrect information or which would have been undercharged if the return or information had been accepted as correct.
>
> (2) Where a person:
>
> (a) makes an incorrect return by omitting or understating any income of which he is required by this Act to make a return on behalf of himself or another person; or
>
> (b) gives any incorrect information in relation to any matter affecting his own chargeability to tax or the chargeability to tax of any other person,

then, if no prosecution under subsection (1) has been instituted in respect of the incorrect return or incorrect information, the Director General may require that person to pay a penalty equal to the amount of tax which has been undercharged in consequence of the incorrect return or incorrect information or which would have been undercharged if the return or information had been accepted as correct; and, if that person pays that penalty (or, where the penalty is abated or remitted under subsection 124(3), so much, if any, of the penalty as has not been abated or remitted), he shall not be liable to be charged on the same facts with an offence under subsection (1).

[36] The SCIT accepted the fact that by virtue of s. 113(2) of the Act, the imposition of the penalty by the respondent on the appellant was not mandatory but an exercise of a discretionary power. The SCIT cited the case of *Ketua Pengarah Hasil Dalam Negeri v. Kim Thye & Co* [1992] 4 CLJ 2079; [1992] 1 CLJ (Rep) 135 as their authority, where the Supreme Court quoted the High Court Judge's statement with approval as follows (at p. 141):

> The learned Judge found from section 113(2) a discretion vested in the Revenue, as to whether to impose or not, a penalty thereunder. His Lordship said:
>
> > … He is given a discretion, a discretion which to my mind he cannot exercise at whim or fancy but after due consideration of all relevant facts and circumstances …

[37] The SCIT then alluded to the respondent's submission that the scheme was never communicated to the respondent and if there was no investigation carried out the scheme would never be discovered, whilst it was the appellant's submission that there was no holding of information since all the sales were duly reported and tax thereon paid. The SCIT nevertheless went on to find that the imposition of the penalty on the appellant was correct in law in the circumstances and that there was no good reason for them to intervene.

[38] Before us, the appellant submitted that the SCIT had:

(a) erred in their interpretation of s. 113(2) in holding that "good faith" was not a defence;

(b) failed to consider the fact that there was no withholding of information since all the sales were duly reported and tax thereon paid;

(c) assumed that the respondent had correctly exercised his discretion without any consideration on whether the penalty was fair and just;

(d) even if the respondent was entitled to involve s. 140 of the Act, the respondent was only entitled to make adjustments with the view to counter the transactions, there is no penalty provided in s. 140 of the Act.

[39] For the respondent, it was submitted that from the facts proven and the evidence adduced, it was clear that there was a scheme executed by the appellant to alter the incidence of tax which was supposed to be paid by the appellant. If the scheme is ruled as unacceptable scheme, it was submitted that the appellant had furnished an incorrect return for failure to disclose all the proceeds from the disposal of the said properties and had given incorrect information in relation to the matter affecting its own chargeability to tax. That under s. 113(2) of the Act, a penalty may be imposed when a person made an incorrect return or incorrect information. Further, the scheme was never communicated to the respondent and if there was no investigation carried out by the respondent, the scheme would never have been discovered. Therefore, failure to disclose such a scheme was an important consideration in the imposition of the penalty. Learned counsel for the respondent referred back to *Challenge Corporation Ltd (supra)* for the proposition that failure to inform all the facts relevant to an assessment can tantamount to tax evasion and not avoidance. In view of all the relevant facts and circumstances of the case, it was submitted that as the appellant had made an incorrect return and information to the respondent, the respondent was correct in imposing a penalty under s. 113(2) of the Act.

The Decision

[40] It is without doubt that s. 113(2) of the Act gives a discretion to the respondent to impose a penalty on a person who has failed to observe the requirements of the law as provided in para. 2(a) or (b) of s. 113. Hence the use of the phrase "the Director General may require that person to pay a penalty". There is a clear distinction between sub-s. 113(1) and sub-s. 113(2). Although paras. 113(1)(a) and (b) and paras. 113(2)(a) and (b) are almost identical, but the effect of sub-s. 113(1) is different from sub-s. 113(2). Sub-section 113(1) provides for an offence being committed in the circumstance provided for in para. (a) or (b) unless that person "satisfies the court that the incorrect return or incorrect information was made or given in good faith". Whereas sub-s. 113(2) provides for a situation where there is no prosecution under sub-s. 113(1) has been instituted in the circumstances provided for in para. 113(2)(a) or (b), the Director General may require that person to pay a penalty. That being the case, the defence of "good faith" as found in sub-s. 113(1), and not found in sub-s. 113(2), does not apply to the Director General's discretion under sub-s. 113(2). We therefore disagree with the appellant's submission on this score.

[41] We also disagree with the appellant's submission that as s. 140 of the Act did not provide for a penalty, the respondent was precluded from invoking it under sub-s. 113(2). It is self evident that s. 140 does not expressly nor impliedly exclude the operation of s. 113. Section 140 gives the discretion to the respondent in certain circumstances and does not relate

to a question of breach by the appellant as such. Neither does the provisions of s. 113 exclude its application in the circumstances provided for under s. 140. Section 113 therefore operates in the circumstances stipulated therein independent of s. 140. Hence we do not find the respondent had erred in invoking s. 113(2) of the Act against the appellant. In not intervening with the respondent's decision to impose the penalty on the appellant, the SCIT had taken into consideration the respondent's submission that if not for the fact that an investigation had been carried out on the appellant and it had stumbled upon the Arthur Andersen's tax advice in 2005, the scheme would never have seen the light of day. In not intervening in the issue of penalty the learned High Court Judge seemed to share the same view. We share the same view. We do not see the need to intervene. We also have in mind the provisions of s. 17A of the Interpretation Acts 1948 and 1967 (Act 388) which require "a construction that would promote the purpose or object underlying the Act (whether that purpose or object is expressly stated in the Act or not) shall be preferred to a construction that would not promote that purpose or object."

Conclusion

[42] For the reasons stated above, we unanimously agree that we see no merits in the appellant's appeal. We therefore dismiss the appeal with costs of RM10,000 to the respondent, unless otherwise agreed. We affirm the decision of the learned High Court Judge when she affirmed the deciding order of the SCIT. Deposit is refunded.